



Issue Brief

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Rising Breakeven Load Factors Threaten Airline Finances

- Since 2000, most large passenger airlines suffered a sharp increase in their Breakeven Load Factor – the number of seats they have to sell to cover operating expenses. Some carriers could not cover operating expenses even if they sold 100% of their seats at average airfares.
- Passenger yield, which partly determines Breakeven Load Factor, has fallen most sharply for recently bankrupt carriers, although it has also declined steeply for most large carriers.
- Unit costs – another factor in Breakeven Load Factor – have been rising for many large passenger airlines. Large airlines at most financial risk had higher unit costs than other airlines even prior to September 11, 2001, and those costs have remained high and have even increased for some.

Breakeven Load Factor (BLF) is the average percent of seats that must be filled on an average flight at current average fares for the airline's passenger revenue to break even with the airline's operating expenses.

Since 2000, most large passenger airlines suffered a sharp increase in their Breakeven Load Factor. Some carriers could not cover operating expenses even if they sold 100% of their seats at average airfares.

This study focuses on three groups of major passenger airlines:

- The “recently bankrupt” – airlines that have filed for bankruptcy within the last two years. This group consists of United Airlines and US Airways. (US Airways has recently emerged from bankruptcy.)
- The “at risk” – airlines that have not filed for bankruptcy, but they have not achieved yearly profits over the last two years. This group consists of American Airlines, Alaska Airlines, Continental Airlines, Delta Air Lines, America West Airlines, and Northwest Airlines.
- The “profitable” – the only major passenger airline to show a yearly profit over the last two years is Southwest Airlines,

The BLFs for the three groups are shown in Figure 1¹.

¹ These airlines comprise all the major airlines except for American Trans Air, which flies a large number of charter flights, and American Eagle, which is a code-sharing partner with American Airlines. The costs and revenues of these two carriers would not be readily comparable with those of other major airlines.

BLFs for the recently bankrupt and at-risk groups began to deteriorate even before September 11th. In Figure 1, the obvious third-quarter 2001 spikes in the BLF reflect the impact of September 11th on the industry.

The most pronounced jump is for the recently bankrupt airlines as that group's BLF increased from 77.7% in the first quarter of 2000 to 114.0% in the first quarter of 2003. For these recently bankrupt airlines, even if they had managed to fill every seat, selling tickets at prices that would have allowed them to remain competitive with other airlines would not have allowed them to generate enough revenue to offset operating expenses.

By contrast, the BLF of the profitable group has stayed below 70%, while the BLF for the at-risk group approached 100%.

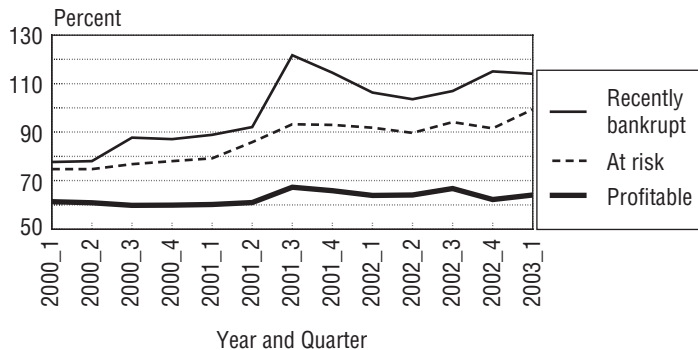
Passenger Yield

Passenger yield, which partly determines Breakeven Load Factor, has fallen most sharply for recently bankrupt carriers, although it has also declined steeply for most large carriers.

A drop in passenger yield for all three groups took place between the first quarter of 2000 and the first quarter of 2003² (Figure 2). The drop is particularly steep for the recently bankrupt group, the group with the highest pas-

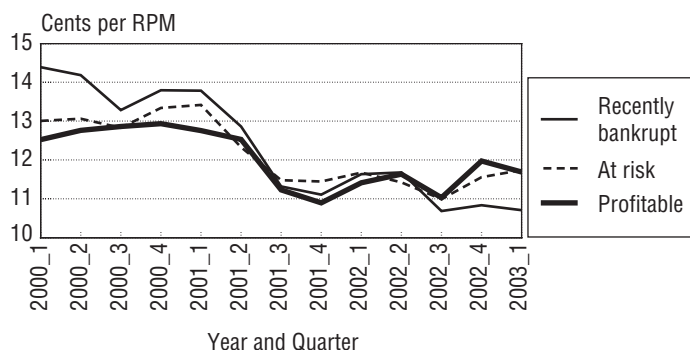
² Passenger yield is determined by dividing the passenger revenue by the number of revenue passenger-miles. The passenger revenue is the amount paid by flying customers. A revenue passenger-mile is one revenue passenger transported one mile.

Figure 1. Quarterly Breakeven Load Factor
(Selected Airlines 2000 to 2003 Q1)



SOURCE: BTS Form 41 Data

Figure 2. Quarterly Passenger Yield
(Selected Airlines 2000 to 2003 Q1)



SOURCE: BTS Form 41 Data

passenger yield in the first quarter of 2000 and the lowest passenger yield in the first quarter of 2003.

The BLF is determined by two variables: 1) unit costs – operating expenses per available seat-mile (ASM), and 2) passenger yield – passenger revenue per revenue passenger-mile (RPM). The BLF is equal to the ratio of these two variables:

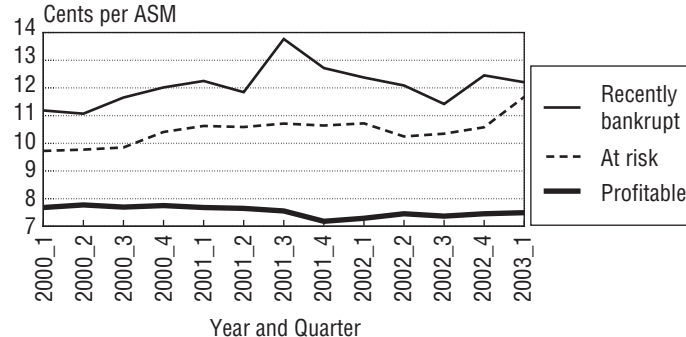
$$\text{BLF} = \text{Unit Cost} / \text{Passenger Yield}.$$

Unit Cost

Unit costs – another factor in Breakeven Load Factor – have been rising for many large passenger airlines. Large airlines at most financial risk had higher unit costs than other airlines even prior to September 11, 2001, and those costs have remained high and have even increased for some.

Unit costs of the recently bankrupt group and the at-risk group exceed the unit costs of the profitable group (Figure 3). Unit costs of the former two groups have been rising (on average) over time, while those for the profitable group have not.

Figure 3. Quarterly Unit Cost
(Selected Airlines 2000 to 2003 Q1)



SOURCE: BTS Form 41 Data

Airlines in the recently bankrupt group and the at-risk group have recently made major cost-cutting decisions. However, the effect of these decisions is not yet reflected in the unit costs because there is a lag between the initiation of cost-cutting initiatives and their effects on operations. Most large carriers cannot implement rapid cost reductions because of contractual obligations and other business constraints.

Because the BLF is the ratio of unit cost to passenger yield, its value can be increased by an increase in unit cost, or a decrease in passenger yield, or both—which is the case for the recently bankrupt group. For this group, the rate of *decrease* in passenger yield is higher than the rate of *increase* of its unit cost. It is primarily this steep decline in passenger yield that caused the BLF of this group to soar well above 100%.

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